GUIDANCE FOR REVIEW OF SCHOOL BUILDING PROJECT FINANCING

Indiana Department of Local Government Finance

On January 19, 2005, Governor Mitchell E. Daniels, Jr., issued Executive Order 05-19 directing the Department of Local Government Finance (the "Department") to

develop guidance to facilitate its review of school building project financings in accordance with IC 6-1.1-19-4.2 and IC 6-1.1-19-8 and to ensure that any such projects are approved only after careful consideration of the factors set forth in IC 6-1.1-19-4.2, including without limitation all matters deemed pertinent by the [Department]. In developing such guidance, the [Department] shall, for example, give due regard to the ratio of academic facilities to non-academic facilities in, and the cost structure of, any proposed school building project financing.

Exec. Order 05-19 (January 19, 2005). Pursuant to that directive, the Department now issues the following Guidance for Review of School Building Project Financing. This guidance is applicable to all new construction and renovation projects coming before the School Property Tax Control Board (the "Control Board") and the Department after January 19, 2005.

PURPOSE OF THIS DOCUMENT

The purpose of the guidance is to provide school officials and other interested parties with the parameters within which the Department and the Control Board will evaluate school construction project financings. This guidance explains how the Department will

assess the merits of a project under the factors set forth in Ind. Code § 6-1.1-19-4.2. The guidance applies to new construction, addition and renovation of public school facilities throughout the State.

School building projects should first and foremost, support the academic needs of the student population. They should also be cost effective in size, construction and per student capacity; minimize maintenance costs; provide a safe and secure working environment for students, staff and administrators; and not be unduly burdensome to taxpayers.

As school officials consider construction projects, the primary focus should be on enhancing academic programs and limiting non-academic space. Their focus should begin with an emphasis on the areas of study required for graduation by the State Board of Education.¹

The Indiana State Board of Education and Indiana Commission for Higher Education recommend a core curriculum of mathematics, science, social studies, language arts, basic physical education, health and safety, and certain directed electives.² Outside the core curriculum are those subject areas connected to an academic program that foster student growth in other areas, including, but not limited to the performing arts, visual arts, CAD-CAM technology or vocational education. Vocational education programs fall into this area rather than the core curriculum because these programs may be offered

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¹ See 511 IAC 6-7-6.1(b)

² Indiana Dept. of Education, Core 40 Overview, http://www.doe.state.in.us/core40/overview.html>.

through other non-public school related entities such as the Community College of Indiana or other accredited programs.

School officials should first consider building projects that provide an environment for students to complete the core curriculum. These instructional programs provide the foundation for students' lives whether they continue their education beyond high school, or immediately enter the work force upon graduation.

The Department and Control Board will evaluate school projects based on a determination of the balance in the amount invested in programmatic development versus extracurricular activities. Projects focused heavily on extracurricular activities will not be automatically deemed infeasible, but rather, they will be subject to greater scrutiny and will require a greater burden of proof regarding necessity. For example, building a vocational education facility for high school students may not be warranted in a community that already has a vocational technical college.

STATUTORILY REQUIRED PROJECT REVIEW

A school corporation must obtain Department approval before it may incur bond indebtedness or enter into a lease agreement for financing a school building project. Ind. Code § 6-1.1-19-8(a). Before it makes a determination, the Department may seek the recommendation of the Control Board. Ind. Code § 6-1.1-19-8(b). The Control Board, when requested by the Department, will hold a hearing on the requested financing and make a recommendation to the Department. The Department may approve, disapprove,

or modify then approve a proposed bond issue or lease rental agreement. Ind. Code § 6-1.1-19-8(b). Factors to be considered by the Department and Control Board are statutorily defined:

[t]he department of local government finance in determining whether to approve or disapprove a school building construction project and the tax control board in determining whether to recommend approval or disapproval of a school building construction project shall consider the following factors:

- (1) The current and proposed square footage of school building space per student.
- (2) Enrollment patterns within the school corporation.
- (3) The age and condition of the current school facilities.
- (4) The cost per square foot of the school building construction project.
- (5) The effect that completion of the school building construction project would have on the school corporation's tax rate.
- (6) Any other pertinent matter.

Ind. Code § 6-1.1-19-4.2. The Department must act on the proposal within the time limits set by Ind. Code § 6-1.1-19-8(c).

The Department and the Control Board will review the facts and circumstances of each school corporation and its proposal as requested on the attached hearing information sheet. This guidance is intended to be broad in scope and to leave discretion with the Commissioner of the Department, to accommodate the varying needs of school corporations throughout the state. The Department will also issue a Report on the State of Indiana School Construction on an annual basis. That document will set numerical thresholds and benchmarks based on the Department's analysis of available data.

I. SQUARE FOOTAGE OF SCHOOL BUILDING SPACE PER STUDENT

Any proposed new building, addition, or renovation project should help to fulfill the school's obligation to provide adequate classroom space to meet program offerings. The Department and Control Board will request information from the petitioning school corporation to determine the impact of the proposed new building, addition, or renovation to the square footage per student in both classroom space and other specialized areas.

The Department and Control Board will consider (1) square footage as compared to current enrollment and current capacity, (2) square footage compared to projected enrollment and new capacity after the proposed project is completed, and (3) the positive and negative impacts of the project on square footage of classroom areas and other specialized areas separately as a reference point for what portion of the project is specifically dedicated to a traditional learning environment. The review of current and proposed square footage per student is to ensure the proposal weighs all internal and external factors affecting the necessary space per student over the school's long term plan in a cost efficient manner.

EXAMPLES:

SCHOOL A has a rapidly increasing enrollment with several large residential developments beginning within the school corporation's boundaries. School A offers a proposal to incur bond indebtedness to build a new high school that will provide additional capacity for 2000 students at 184 square feet per student. School A comes before the Control Board and Department and demonstrates that the new high school proposal creates this additional square footage per student in order to accommodate future growth in a cost efficient manner. School A provides

the Control Board and Department with studies showing the increasing population of the area and the projected effect on the high school enrollment over a significant period of time. Assuming that School A's project conforms to the other provisions of this guidance, this proposal would likely be approved.

SCHOOL B offers a lease agreement proposal that expands five existing classrooms by a total of 1000 square feet. School B appears before the Control Board and demonstrates how the extra classroom space will be used to accommodate necessary updates to science labs and computer classrooms. Assuming that School B's project conforms to the other provisions of this guidance, this proposal would likely be approved.

SCHOOL C presents a bond proposal for a project that will expand non-academic facilities that are adjacent to the school. The school has an immediate need for additional classrooms due to overcrowding, but has chosen not to address that problem with this project. If the school's need for classroom space exceeds the need for non-academic space, a project that addresses only non-academic space would likely be denied.

II. ENROLLMENT PATTERNS WITHIN THE SCHOOL CORPORATION

Projects submitted to the Department and Control Board for approval should include as much information as possible regarding recent enrollment patterns by grade and supporting long-term projections of future enrollment. Projects should be consistent with enrollment trends and migration patterns within the district. If enrollment patterns by grade show a clear need for additional classroom space or additional school buildings, reasonably cost efficient projects satisfying that need will likely be approved.

Current facility enrollment and capacity will be compared to projected enrollment and new facility capacity established by the proposed project. It is important that school corporations present as much information as possible regarding enrollment trends. They must explain the impact of those trends on the on their project proposal. Such

information should include population or demographic studies of the area, details regarding new or proposed residential and business developments in the district, as well as any other probative information.

EXAMPLES:

SCHOOL D and SCHOOL E are in adjacent districts. Both have declining enrollments. The Schools present a project that involves consolidation of their two high schools into one new high school building in a centralized area. They present studies showing how consolidation best serves the students, the community, and the taxpayers. Assuming that their project conforms to the other provisions of this guidance, this proposal would likely be approved.

SCHOOL F has a rapidly increasing enrollment. It presents a plan to build a new elementary school that will accommodate 200 students. Other elementary schools in the district accommodate 600 students and are already at or above capacity. If the 200 student school is built, it may quickly become overcrowded and necessitate another new building. Because this facility does not adequately address the increasing enrollment problem facing the district, it may be denied or approved only after modification.

III. AGE AND CONDITION OF CURRENT SCHOOL FACILITIES

Of foremost concern is the capability of the facilities to provide a safe and secure learning environment for the students. School corporations will be asked to present detailed descriptions of the age and condition of their existing facilities. The Department and Control Board will review whether the facilities are nearing the end of their useful life and should be remodeled, replaced, or whether the facilities should continue to be used.

Proposals to bring facilities up to minimum safety, health, or security standards in a cost efficient manner will likely be approved by the Department and Control Board in an expedited manner. School corporations will be asked to identify each of their current facilities by age and classify them according to the following criteria:³

Excellent

Buildings of quality construction, of good design to meet educational needs, and flexible enough to accommodate changing educational programs. Excellent physical condition. Modern mechanical systems with air conditioning typical. The school meets all ADA requirements. Analysis will indicate that renovation or additions are feasible, if necessary.

Very Good

Buildings of sound construction, above average condition, adequate in design for required educational programs and affords flexibility to accommodate changing educational programs. Analysis will indicate renovation is feasible. The building meets building code requirements. Mechanical systems are adequate and not expected to deteriorate in the short term.

Good

Buildings of average construction, which meet minimum building code requirements. The building is expected to accommodate short-term needs, but may be limited in its ability to provide accommodations for all educational programs. The building may also not meet ADA requirements. Mechanical systems are average. Analysis indicates renovation is usually feasible.

Fair

Buildings that are marginal in construction and condition. Building design accommodates short-term needs and inadequate to meet education programs. The building does not meet present day construction codes and may not provide accommodations for the disabled. The building typically is maintained for health and safety purposes, but should be replaced.

Poor

Buildings that are structurally or educationally inadequate in construction, design and flexibility. The building does not meet present day construction codes, including ADA

³ North Carolina State Dept. of Public Education, *Cost and Feasibility of Renovating or Replacing an Old School Building* at 2, (Apr 8, 1998) http://www.schoolclearinghouse.org/pubs/costfeas.pdf>.

accessibility. Mechanical systems are not feasible, outdated and costly to replace. Feasibility and cost analysis indicate renovation is not an acceptable alternative, but replacement more appropriate. The building should be phased out in the short-term.

EXAMPLES:

SCHOOL G has a deteriorating high school building that is 70 years old. The building's mechanical systems are outdated and will be costly to replace. The building does not meet state construction codes or ADA accessibility standards. School G presents a proposal for a \$100 million renovation project to put the building into good overall condition. Even after completion of the renovation project, the school will still incur substantial maintenance costs. School G has also studied the cost of replacing the current building with a new facility and estimated that cost to be \$50 million. School G decided to pursue the renovation project because the community prefers to keep the older building. Because the renovation proposal does not resolve the facility age and condition problems in a cost-efficient manner, this project would likely be denied or approved only after modification.

SCHOOL H has a building with a collapsing roof. The school building has no other structural problems. The school corporation presents a project that will repair the roof in an expedited manner. Because of the necessity of the repairs, the project would likely be approved if this project conforms to the other provisions of this guidance.

IV. COST PER SQUARE FOOT OF THE SCHOOL BUILDING PROJECT

The Department and Control Board will review the project's proposed cost per square foot estimates to ensure the project is done in a cost efficient manner. The Department has developed and will maintain a database of project cost per square foot at both the schematic design stage and contract award stage. The Department will compile an Annual Report on the State of Indiana School Construction. The report will include all projects proposed, approved, and completed in Indiana and compare those projects to

regional and national data. This information will be used to evaluate whether each project falls within a reasonable range when compared to similar projects throughout the state, region, and nation. If proposed projects are above the thresholds established by that data, those projects will receive greater scrutiny and may be denied unless or until the school provides additional information regarding the reasons for the increased cost and explains why the increased costs are necessary to the school's educational program.

The Department and Control Board will also review the project financing structure to determine whether the soft costs such as advisor fees, counsel fees, and architect fees for the project fall within a reasonable range when compared to other Indiana projects. As with construction costs, soft costs that are dramatically outside of a reasonable range will require additional information or project modification.

School corporations requesting approval to construct new buildings will be asked to provide studies regarding the feasibility of addition to, or remodeling of, existing facilities in lieu of new construction. If an analysis of the cost difference between new construction and addition has been performed, that analysis should also be provided to the Department and Control Board.

EXAMPLES:

SCHOOL I presents a proposed lease agreement for a new elementary school building that has a calculated construction cost 10% higher than the high end of the Department data range for new elementary schools. School I officials explain that the increased cost is due to the use of a high-tech HVAC system that will increase construction costs, but will significantly decrease operating costs over the life of the school. School I

presents studies showing that the projected savings over time will more than offset the excessive construction cost. Assuming that the School I project is conforms to the other provisions of this guidance, this proposal would likely be approved.

SCHOOL J presents a project to the Department that uses very elaborate and expensive materials in its new school building so that the building will be aesthetically pleasing. School J cannot explain why the expensive materials are required over less expensive alternatives. School J's project would likely be denied because it does not represent an efficient use of taxpayer funds.

V. EFFECT OF THE PROJECT ON THE SCHOOL CORPORATION'S TAX RATE

The Department and Control Board will look to the totality of the circumstances in evaluating the impact of a project on tax rates within the school corporation's district. In addition to construction costs, school corporations should anticipate and offer information regarding possible need to impose an additional levy for ongoing operating costs for the new or expanded facility. The Department and Control Board will also consider any other pending or potential debt service issues by other political subdivisions within the school district and the impact of those debt issues on the total tax rate. Every project will have some impact on the tax rates within the school corporation's boundaries. If the tax rate for a district is already overly burdensome, a project may be rejected with instructions to find a more cost-efficient alternative to addressing the school's needs.

The Department and Control Board will also look at the repayment schedule and structure of the debt incurred by the school corporation and may reject plans that involve extreme balloon payments and subsequently higher interest costs, or the substitution of new debt when existing debt drops off if the public has not been properly informed about

the debt service rate impact. A school's annual financial performance report will also be considered in reviewing the district's overall financial condition and ability to fund long term operating costs.

EXAMPLES:

SCHOOL K proposes a new middle school project that involves a \$46 million bond issue paid over the course of 20 years. The payments are very low for years one through nineteen, but require a sizable balloon payment in year twenty to retire the bonds. The balloon payment structure causes the school corporation to be liable for an additional \$10 million in interest over the course of the bonds. Because of this wasteful use of taxpayer funds, School K's proposed financing would likely be denied.

SCHOOL L proposes a new school building project that uses an innovative wraparound structure that lowers the cost of financing. School L demonstrates to the Department and the Control Board that the debt structure is a prudent use of taxpayer dollars because of the reduced financing cost. Assuming that the School L project is conforms to the other provisions of this guidance, this proposal would likely be approved because it significantly reduces the interest cost.

VI. ANY OTHER PERTINENT MATTER

Under Ind. Code § 6-1.1-19-4.2(6), the Department and Control Board are required to review projects for any other matter pertinent to the approval or disapproval of a school building construction project. The Department and Control Board will consider, among other things, the percentage of a project that is for academic facilities versus non-academic facilities, academic performance within the school corporation, the support or resistance of the community, and the long term plans of the school corporation.

a) Academic vs. Non-Academic Facility Spending

In evaluating a project, the Department and Control Board will use the schematic design, the project description, information from the hearing information sheet, and testimony presented at the Control Board hearing to discern which portions of the proposed facilities will be dedicated solely to academic uses, which portions of the facilities will be used for both academic and non-academic purposes, and which portions of the facilities will be used entirely for non-academic purposes. Projects that have a majority of their use falling into the latter two categories will meet a higher level of scrutiny and burden of proof regarding necessity.

For projects that involve facilities not dedicated solely to academic use, inquiries will be made to determine if (1) the school corporation has addressed all of its academic facility needs, (2) there is an urgent need for the facility, and, (3) the proposal is the most cost-efficient means of addressing the school's need.

b) Academic Performance

The Department and Control Board will look at several factors that reflect on student achievement within the district including, but not limited to, persistence to graduation, ISTEP scores, percentage of students taking "Core 40" required courses, advance placement courses offered, curriculum programs and course offerings, and percentage of students taking math and science classes. If a school corporation is having trouble meeting its academic performance goals, it is less likely the Department and the Control

Board will approve a project that does not provide the proper environment to address those concerns.

c) Community Support or Resistance

The Department and Control Board will consider local concerns as part of its decision-making process. In order to assist the Department and Control Board in determining the community and taxpayer positions regarding a proposed project, the Department and Control Board will require that all written material held by the school corporation that expresses support for, or opposition to, the project be presented at the Control Board hearing. School corporations should also disclose alterations or concessions that have been made to the project as a result of public comment. Taxpayers will be able to submit their comments in writing prior to or during the hearing.

d) The Long Term Plan for the School Corporation

The Department and Control Board will review the long-term educational plans and building needs for the school corporation to determine if (1) this project is consistent with the long term plans for the school district, (2) there are more immediate needs not being addressed by this proposal, and (3) whether, given current circumstances, the money needed for the proposal is being spent in a way the best serves the educational purpose of the school corporation and does not overly burden the taxpayers.

ADDITIONAL STATUTORY CONSIDERATIONS

For projects involving the construction of additional classrooms, the Department may not approve a project unless the school corporation first establishes the necessity of the additional classroom space and conducts a feasibility study, including holding a public hearing, regarding the feasibility of a twelve-month school year rather than an expansion of classroom space. Ind. Code § 6-1.1-19-8(d).

If a school corporation has prepared a feasibility study reviewing proposed sources of funding and estimated impact on tax rates for projects over one million dollars under Ind. Code § 20-5-52-1, that study should be presented to the Department.

CONCLUSION

The importance of developing school building projects that foster a challenging and rewarding academic environment for students cannot be underestimated. This guidance is not an exhaustive list of factors that will be examined and considered by the Department and the Control Board. The guidance is intentionally broad in scope and leaves discretion with the Commissioner of the Department in recognition of the fact that school corporation needs vary throughout the state. The Department's focus is to assist schools in finding the appropriate balance between academic and non-academic spending in each project.